



A Synopsis of the New Rules on Issuance, Offering Platforms, and Custody of Digital Assets

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Background

On 11 May 2022, as part of its efforts to effectively regulate digital/virtual assets in Nigeria, the Securities and Exchange Commission (the “Commission”) released new rules for Digital Assets. The new rules which it named “New Rules on Issuance, Offering Platforms, and Custody of Digital Assets” (the “New Rules”) are in furtherance to the earlier released Proposed Rules for the Registration of Virtual Assets Providers in Nigeria and the Proposed Rules on Issuance, Offering Platforms, and Custody of Digital Assets. In this article, we have provided a synopsis of these New Rules.

The New Rules are divided into the following parts:

1. Part A - Rules on Issuance of Digital Assets as Securities;
2. Part B - Rules on Registration Requirement for Digital Assets Offering Platforms (DAOPs);
3. Part C - Rules on Registration Requirements for Digital Asset Custodians (DACs);
4. Part D - Rules on Virtual Assets Service Providers (VASPs); and
5. Part E - Rules on Digital Assets Exchange (DAX).

RULES ON ISSUANCE OF DIGITAL ASSETS AS SECURITIES

The New Rules apply to all issuers seeking to raise capital through digital asset offerings. Digital Asset is defined as a digital token that represents assets such as a debt or equity claim on the issuer.¹

The New Rules provide that, except in cases of follow-on offerings, all promoters, entities, or businesses proposing to conduct initial digital asset offerings within Nigeria or targeting Nigerians, shall submit an assessment form and draft whitepaper to the Commission. The whitepaper² requires a statement in bold letters thus:³

¹ Rule 2

² A document that states the technology behind a project, including a detailed description of the system architecture and interaction with the users, description of the project and use of proceeds, information on the market capitalisation, anticipated growth, other technical details and the team and advisors behind the project.

³ Rule 4

“THE SECURITIES AND EXCHANGE COMMISSION HAS NOT APPROVED THESE TOKENS OR DETERMINED IF THE TOKENS ARE SECURITIES AND THUS, SHALL BE REGISTERED, OR THAT THE CONTENT OF THE WHITEPAPER ARE ACCURATE AND COMPLETE. ANY FALSE OR MISLEADING REPRESENTATION IS A CRIMINAL OFFENCE AND SHOULD BE REPORTED IMMEDIATELY TO THE SECURITIES AND EXCHANGE COMMISSION”.



The Commission has 30 days from the receipt of a complete initial assessment filing, to determine whether the digital asset to be offered, constitutes a “security” under the Investment and Securities Act 2007 (“the Act”) and such determination shall be communicated in writing to the issuer within 5 days from the conclusion of the review.⁴ The fixing of deadlines for the determination and communication by the Commission is a commendable addition as it will make the process less protracted due to administrative delays and bureaucracy. Upon determination as a security, the issuer of the digital asset shall apply to register the said securities.

1.1. Registration Requirements for Digital Asset Offering

Upon determination by the Commission that the proposed digital assets to be offered are securities, the issuer shall file an application for registration. Such application shall include the Commission’s minimum disclosure requirements for public offers in addition to other requirements listed out in the Act. Where the issuer complies with the registration requirements, the Commission may grant registration of the digital assets. However, the Commission may reject such application if in its opinion, the proposed activity infringes public policy, is injurious to investors or violates any of the laws, rules and regulations implemented by the Commission.⁵

We note that compliance of the issuer with the registration requirements does not automatically guarantee registration by the Commission of the digital assets. The Commission reserves the right to justify its decision on other factors. It is germane that the Commission exercises this power judiciously in the interest of the investors, issuers, and the general public.



⁴Rule 4

⁵Rule 5

1.2. Limits of Funds to be Raised/Investment Limits

The issuer shall demonstrate that the gross proceeds to be raised from the digital asset offering will be sufficient to undertake the project as proposed in the whitepaper and in the event that the amount raised is below the soft-cap⁶, the issuer shall refund all monies collected from the token holders within five (5) business days from the offer closing date.⁷

This provision helps to ensure the refund of investors' funds in the event that the amount raised is insufficient for the project. We believe this is a calculated attempt at preventing some individuals who may want to use this as an avenue to unjustly enrich themselves at the expense of the investors.

There are no restrictions in the New Rules regarding the investment amount for qualified institutional and high net worth investors. However, for retail investors, a maximum of N200,000.00 (Two Hundred Thousand Naira) per issue with a total investment limit not exceeding N2,000,000.00 (Two Million Naira) within a 12-month period.⁸



REGISTRATION REQUIREMENTS FOR DIGITAL ASSETS OFFERING PLATFORMS

“Digital Assets Offering Platform” (“DAOP”) is defined in the New Rules as an electronic platform operated by DAOP operator for offering digital assets.

2.1. Registration Requirements

Under the New Rules, an applicant seeking to register a DAOP shall, in addition to the general requirements for Virtual Assets Service Providers (“VASPs”)⁹, comply with the following requirements:¹⁰

- (a) Payment of prescribed fees;
- (b) Application to be made on the appropriate SEC Form;
- (c) Evidence of minimum paid-up capital and current fidelity bond;¹¹
- (d) Compliance with the requirements for registration of sponsored individuals as contained in the SEC Rules and Regulations;
- (e) Provision of corporate documents;¹²
- (f) Additional requirements include a copy of draft rules of the DAOP, sworn undertaking to promptly furnish the Commission with copies of any amendments to the rules of the DAOP, information on the company, sworn undertaking to keep proper records and returns signed by a director or the company secretary, and sworn undertaking to abide by SEC Rules and Regulations and the Act by a director or the company secretary.¹³ The undertakings shall be stamped with the stamp of the Commissioner for Oath or notarised by a notary public.

⁶The minimum amount of funds needed and aimed by the project to proceed as planned.

⁷Rule 7

⁸Rule 8

⁹Virtual Assets Service Providers (discussed under Part 4)

¹⁰Rule 11

¹¹Minimum paid-up capital is N500,000,000.00 (Five Hundred Million Naira) only, i.e., bank balances, fixed assets, or investment in quoted Securities. Current fidelity bond must cover 25% of the minimum paid-up capital. Notwithstanding the provision relating to minimum paid-up capital, Commission may at any time impose additional financial requirements on the DAOP commensurate with the nature, operations and risks posed by the DAOP. See Rule 11.4(c)

¹²A copy each of the following duly certified by the CAC – Certificate of Incorporation (original to be sighted); Memorandum and Articles of Association which shall include the power to perform the specified function; CAC Form(s) showing statement of share capital, return of allotment, and particulars of directors; Latest audited accounts or audited statement of affairs of the company in the case of a new company; Tax Identification Number Clearance Certificate; Such other documents as the Commission may consider.

Applicants shall endeavour to provide all documents listed above to ensure that processing of the application proceeds and is duly registered.

2.2. Governance

The DAOP shall have a Board and Management charter that clearly stipulates responsibilities.¹⁴ A DAOP shall have a Board whose appointment shall be subject to approval by the Commission before registration at the CAC. The Chief Executive Officer (CEO) of a DAOP shall hold office for a maximum period of ten (10) years.¹⁵ The appointment of the CEO and other principal officers shall be subject to the approval of the Commission. The CEO and other principal officers shall, among other requirements, be registered as Sponsored Individuals with the Commission.



2.3. Conflict of Interest Management

A DAOP, including its directors and shareholders shall disclose to the public on its platform if it holds any shares in any of the issuers or virtual assets/digital tokens issued by any issuers hosted on its platform, or if it pays any referrer or introducer, or receives payment in whatever form, including payment in the form of shares, in connection with an issuer hosted on its platform. Our understanding of this provision is that this duty is only limited to disclosure.

Notwithstanding the above, DAOP's shareholding in any of the issuers hosted on its platform shall not exceed thirty (30) per cent, subject to the approval of the Commission. A DAOP is also prohibited from providing direct or indirect financial assistance to investors to invest in the virtual assets/digital tokens of an issuer hosted on its platform.¹⁶ We believe this provision is necessary for transparency purposes.



¹⁴Rules 13, 14, and 15

¹⁵A period of five (5) years in the first instance and may be re-appointed for a further period of five (5) years and no more.

¹⁶Rule 19

2.4. Custody of Virtual asset/Digital token

The New Rules permit the DAOP to appoint a digital asset custodian registered with the Commission to provide custody of the token holders' virtual assets/digital tokens. A DAOP also has the option of choosing to provide its own custody services to the token holder, in which case the DAOP shall comply with the Requirements for Digital Asset Custodian set out under the Rules.¹⁷ The provision for a digital asset custodian will help instill confidence in investors as this will provide a degree of transparency and structure.

REGISTRATION REQUIEMENTS FOR DIGITAL ASSET CUSTODIANS



“Digital Asset Custodian” (DAC) under the New Rules is defined as a person who provides the services of providing safekeeping, storing, holding, or maintaining custody of virtual assets/digital tokens for the account of another person.

3.1. Registration Requirements

To be registered as a DAC under the New Rules, the following requirements must be complied with:

- (a) satisfy eligibility requirements for registration as a Custodian or Trustee, and any additional requirements which the Commission may prescribe from time to time;
- (b) where a registered Custodian or registered Trustee seeks to provide DAC services, such CMO shall apply to the Commission for approval;
- (c) payment of fees as prescribed by the Commission;
- (d) fulfil the general requirements for VASPs.

In addition, the New Rules provide that the Commission may register a foreign DAC, provided that the applicant fulfils requirements set out in the New Rules and the Commission is, in addition, satisfied that the applicant is authorised to operate or carry out an activity of a similar nature in the foreign jurisdiction, and the applicant is from a comparable jurisdiction with whom the Commission has regulatory arrangements on enforcement, supervision, and sharing of information.¹⁸

¹⁷Rule 21

¹⁸Rule 30

A DAC shall prioritise the client's interest in the event of conflict and shall ensure that all clients' virtual assets/digital tokens are properly segregated from its own assets and safeguarded from conversion or inappropriate use by any person. This provision provides assurances to the investor that its assets are adequately protected and safeguarded from unauthorised or illegal use.

RULES ON VIRTUAL ASSETS SERVICE PROVIDERS



The rules on virtual assets service providers, as provided in the New Rules, apply generally. This means that its requirements are generally applicable to other parts. The rules cover the following:

- (a) Requirements for Registration of VASPs;
- (b) Requirements for Registration of a Digital Asset Exchange;
- (c) Requirements for Registration of a Digital Asset Custodian;
- (d) Requirements for Registration of Digital Asset Offering Platform;
- (e) Requirements for Issuance of Digital Assets

The New Rules provide that these rules shall be read in conjunction with all relevant and applicable laws and the Rules and Regulations of the Commission and that it shall apply to the following: ¹⁹

- (a) all platforms that facilitate trading, exchange, and transfer of virtual assets;
- (b) any person (individual or corporate) whose activities involve any aspect of Distributed Ledger Technology (DLT)-related and virtual digital assets services. Such services include but are not limited to reception, transmission, and execution of orders on behalf of other persons, dealers on own account, portfolio management, investment advice, custodian or nominee services, etc.;
- (c) issuers or sponsors of virtual/digital assets, including foreign or non-residential; and
- (d) foreign or non-residential operators that actively target Nigerian investors directly or through their agents, through promotions, publications in Nigeria or direct e-mails to Nigerian addresses.

¹⁹Part D, Rule 1

According to the New Rules, a VASP shall be structured as a body corporate unless specified otherwise by the Commission.

- (a) a technology service provider who merely provides the infrastructure, software, or system to a Digital Asset Exchange (DAX);
- (b) an operator of a communication infrastructure that merely enables orders to be routed to an Exchange;
- (c) an operator of a financial portal that aggregates content and provides links to financial sites of service and information provider.

4.1. Requirements for registration

Application for registration as a VASP shall be filed on the appropriate SEC Form contained in the applicable Schedule to the SEC Rules and Regulations 2013 and accompanied by the relevant documents.²⁰

Another very important requirement is the presence of an office in Nigeria managed by a director of the company.

The obligations of a VASP are clearly spelt out in Rule 5.1 of Part D of the New Rules.

RULES ON DIGITAL ASSETS EXCHANGE



5.1. Requirements for registration

Under the New Rules, an applicant seeking to register as a DAX Operator shall comply with the following requirements:²¹

²⁰Please see Part D, Rule 4.1 for the relevant documents

²¹Please note that this is in addition to the general requirements for VASPs. Please see Part E, Rules 6, 7, and 8

- (a) Payment of the prescribed fees;
- (b) Application to be made on appropriate SEC forms;
- (c) Evidence of minimum paid-up capital and fidelity bond ²²
- (d) Compliance with the requirements for registration of sponsored individuals as contained in the SEC Rules and Regulations;
- (e) Provision of corporate documents;²³
- (f) Additional requirements include sworn undertaking to keep proper records and render returns and to abide by SEC Rules and Regulations and the Act by a director or the company secretary. The undertakings shall be stamped with the stamp of the Commissioner for Oath or notarised by a notary public.

Applicants shall endeavour to provide all documents listed above to ensure that processing of the application proceeds and is duly registered.

5.2. Governance

The DAX Platform has similar governance structure as the DAOP discussed above.

Conclusion

The release of the New Rules by the Commission is indeed a step in the right direction in its quest to effectively regulate digital/virtual assets in Nigeria. It has offered an effective framework for digital/virtual assets to be brought within the broader securities' regulatory framework in Nigeria. The provisions on Digital Assets Custodian will no doubt increase investors' confidence with the resultant effect being more investment in the Nigerian economy.

However, the current instruction by the Central Bank of Nigeria (CBN) to banks and other financial institutions prohibiting transactions in digital assets (cryptocurrency) and facilitating payments for same may serve to avert the effectiveness of the New Rules. Until the CBN sets aside this instruction, the New Rules may be futile.

In any case, it is our hope that the provisions of the New Rules will be stringently observed by the relevant stakeholders to enable Nigeria benefit from the prospects embedded therein.

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²² Minimum paid-up capital is N500,00,000 (Five Hundred Million Naira) (i.e., Bank balances, Fixed asset or investment in quoted securities) Current fidelity bond must cover at least 25% of the minimum paid-up capital as stipulated by the Commission's Rules and Regulations. Please note that the Commission may at any time impose additional financial requirements or other terms and conditions on the DAX Operator that commensurate with the nature, operations, and risks posed by the DAX Operator. In addition, all funds shall be made through Real-Time Gross Settlement (RTGS)

²³ A copy each of the following, duly certified by the CAC – Certificate of Incorporation (original to be sighted); Memorandum and Articles of Association which shall include the power to perform the specified function; CAC Form(s) showing statement of share capital, return of allotment, and particulars of directors; Latest audited accounts or audited statement of affairs of the company in the case of a new company.